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## Hong Kong: Sino-British Disputes and Implications for U.S. Interests

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## Hong Kong: Sino-British Disputes and Implications for U.S. Interests

### SUMMARY

On Oct. 7, 1992, Hong Kong's new Governor, Christopher F. Patten, unveiled a set of proposals to expand the voting franchise in Hong Kong and broaden the scope of other democratic initiatives. The People's Republic of China, which resumes sovereignty over Hong Kong on July 1, 1997, has objected strenuously to the proposals, claiming they are a violation of the 1984 Sino-British Joint Declaration on the Question of Hong Kong. British and Hong Kong officials deny this, stating that the proposals deal with matters not mentioned in the Joint Declaration.

Patten's proposals are in line with general U.S. goals of promoting human rights and political liberalization, and with the more particular U.S. goal of maintaining Hong Kong's autonomy to the maximum extent possible after it reverts to Chinese control in 1997. But the confrontation with China over Patten's proposals has created a crisis that seriously threatens American economic interests and possibly U.S. political objectives as well. Beijing has said that unless Patten withdraws his proposals, China may dissolve Hong Kong's legislature upon resuming sovereignty. Chinese officials also have stated that if Patten's proposals are approved, then Beijing will ignore the Joint Declaration and will find all contracts, leases, and agreements signed or certified by the Hong Kong government without Beijing's approval to be invalid after 1997.

Governor Patten formally incorporated his proposals into legislation on March 13, 1993, and he has stated that he intends to present the reform bill to Hong Kong's legislature, the Legislative Council (Legco) for consideration. But Hong Kong authorities repeatedly postponed their self-imposed

deadlines for submitting the proposals to Legco, reportedly awaiting word from British officials trying to engage Beijing in negotiations on the reform package. After much controversy, China and Britain on Apr. 22, 1993, began to hold talks about the reform package. Although the willingness of both sides to negotiate originally raised the expectations in Hong Kong that a compromise would be reached, those hopes have faded as the talks, after seventeen frustrating rounds, appear to have broken down. On Dec. 2, 1993, Governor Patten formally announced that he would submit part of his political reform proposals to Legco without having received China's endorsement of the proposals. Chinese officials, in response, have publicly stated that Patten's decision amounts to a unilateral break-off of negotiations, and that China will not honor any legislation that is enacted by Legco without Beijing's approval.

In 1992, the U.S. Congress enacted legislation which spells out the objectives for U.S. policy toward Hong Kong, requires a regular report by the State Department on political and human rights progress in Hong Kong (the first report was released in March 1993), and permits the President to suspend agreements with Hong Kong after 1997 if he determines that China is not granting the territory sufficient autonomy. The current dispute places U.S. policymakers in the difficult position of having to balance a number of competing U.S. policy goals, including: U.S. economic interests and global competitiveness; U.S. bilateral relations with China and Britain; U.S. support for democratization initiatives in Eastern Europe and former Soviet republics; and U.S. commitments to human rights and self-determination.

## **MOST RECENT DEVELOPMENTS**

*On Feb. 24, 1994, China announced that it would dissolve Hong Kong's elective bodies, including the legislature, when China resumes sovereignty over the colony in 1997. The blunt statement came in retaliation for Governor Chris Patten's decision to introduce a second legislative reform package to Hong Kong's Legislative Council (Legco). On February 23, Legco had adopted the first phase of Governor Patten's political reform proposals, which he had submitted as legislation on Dec. 15, 1993. That new law has lowered the voting age in Hong Kong to age 18; created single-seat, single-vote elections for Legco, district boards, and municipal councils; and abolished appointed seats for local-level governing bodies. The reform arrangements have been the subject of months of heated negotiations between Britain and China, which has strenuously objected to the Patten reform proposals. When negotiations on the proposals broke down in late November 1993 after 17 rounds of talks, Governor Patten made the decision to introduce the reform package to Legco unilaterally, without Beijing's approval.*

## **BACKGROUND AND ANALYSIS**

### **U.S. Stake in Hong Kong**

The economic interests of a number of countries intersect in Hong Kong. China is Hong Kong's largest investor, while Japan vies with the United States as the second largest. By 1992, U.S. investments in Hong Kong reached \$7 billion. Approximately 900 U.S. firms have corporate offices in Hong Kong, most of which are used as financial and marketing bases in support of substantial production facilities in neighboring China, and as headquarters for business activities throughout Asia. About 44 U.S. banks have entities operating in Hong Kong. Altogether, about 25,000 Americans live and work in various U.S. private and government enterprises in Hong Kong -- the largest group of expatriates in the colony. U.S. multinational companies have played a large role in organizing production in Hong Kong and neighboring Guangdong Province in southern China, which has become the economic hinterland and manufacturing base for Hong Kong. The United States is Hong Kong's largest market, importing almost \$10 billion worth of goods from the territory in 1992. Hong Kong is the twelfth largest U.S. export market, importing approximately \$9 billion in U.S. goods in 1992.

### **Past British-Chinese Negotiations: Joint Declaration and Basic Law**

The current dispute is the most serious in a series of Sino-British negotiations and disagreements since 1984 over governing Hong Kong and arranging for its future political system after China resumes sovereignty on July 1, 1997. Under the Sino-British Joint Declaration of 1984, which calls for returning Hong Kong to China without a self-determination referendum, the method for selecting Hong Kong's future political leaders was to be governed by the provisions of a Basic Law that would serve as the territory's de-facto constitution after 1997. Negotiations over plans for the Basic Law were prolonged and controversial. Britain, responsible for administering Hong Kong through June 1997, generally tried to push for as much autonomy as possible for the territory. Among other

things, British negotiators proposed instituting direct elections for Hong Kong's legislature, the Legislative Council (Legco). China opposed these efforts, saying they were attempts to interfere with China's ability to administer Hong Kong after 1997. China clearly prefers that Hong Kong have a strong Executive and a weak, appointed legislature -- conditions, Chinese leaders have pointed out, that have existed in Hong Kong under nearly a century of British rule.

With the adoption of the Basic Law finally on Apr. 4, 1990, many of these matters appeared to be resolved, although not without continuing controversy. The Basic Law provided that the Hong Kong Legislative Council "shall be constituted by elections." Elections were to be implemented gradually, with the ultimate aim stated to be electing all of Legco through universal suffrage. In 1991, 18 out of 60 Legco seats were opened for direct elections, and this number is to grow eventually to 30 directly elected seats (out of 60) by the year 2003. The initial figure of 18 was regarded as China's figure -- one which the British Government officially accepted with reservations, and which British officials stated publicly they would continue efforts to expand upon. (For further details on Legco and its makeup, see CRS Report 92-525, *Hong Kong: Political and Economic Issues*, by Kerry Dumbaugh).

Despite the adoption of the Basic Law, Sino-British interaction over Hong Kong has remained troubled over the extent of influence Beijing should have over economic and political decisionmaking in Hong Kong prior to and after 1997. The Joint Declaration says only that Britain will administer Hong Kong until 1997, and that China will cooperate. In part, tensions over China's role may reflect greater British sensitivity to criticism that its impending handover of Hong Kong to communist China appears increasingly out of step with recent global events, including the demise of Soviet communism. Some believe that these factors combined in 1992 to convince Britain it should abandon its more conciliatory tone of the past and seek indirectly to limit Beijing's role in the colony. Others suggest that Prime Minister John Major appointed Patten to replace Hong Kong Governor David Wilson for more traditional political considerations -- to reward a close friend who was defeated in his own bid for reelection to Parliament -- and that Patten in turn is simply pursuing his own political agenda.

## **Patten Reform Proposals**

Christopher F. Patten, sworn in as Hong Kong's 28th Governor on July 9, 1992, is regarded as a break in the tradition of British Hong Kong Governors. He is aggressive and plain-spoken rather than aloof and reserved. Unlike many of his predecessors, he is not a China scholar; he is instead a practiced politician and, as former leader of the British Conservative Party, one of considerable stature and influence. Patten is also a close confidante of Prime Minister Major, and engineered the Prime Minister's most recent election victory. From the beginning, Beijing was disturbed by his appointment, interpreting it as an indication that Britain would be pursuing a tougher line in Hong Kong.

On Oct. 7, 1992, in his first annual Governor's Policy Address to Legco, Patten described a five-year plan for economic and political reforms for Hong Kong. Under the heading of "Constitutional Development," Patten described a number of steps which he termed were for the purpose of "building up democracy in Hong Kong." He also announced that he would submit his reform package to Legco for consideration, amendment, and

final action. On Feb. 23, 1994, Legco considered and approved the first of two electoral reform bills; on Feb. 25, 1994, a second set of proposals was incorporated into legislation, scheduled for consideration by Legco later in March.

By Western standards, the proposals seemed mild. Patten did not propose increasing the number of directly elected seats in Legco -- something which was spelled out in the Basic Law -- but instead opted for a series of steps to institutionalize other procedures on which the Joint Declaration and the Basic Law were silent. Patten's proposals included the following:~

Patten's Proposal	Status Quo/China's Position
Expand the number of functional constituencies in Legco to 30, and broaden their franchises to include a wider range of workers within each profession <sup>2</sup>	Currently there are 15 functional constituencies with membership limited to elite in the profession -- i.e. to lawyers, but not to paralegals or legal secretaries; Beijing has agreed to 30 functional constituencies, but not to their expanded franchise
Abolish appointed members to Municipal Councils and District Boards and expand District Board jurisdiction <sup>1</sup>	Currently, some members are elected and others are appointed by the Governor.
Abolish the tradition of appointing some Legco members to serve concurrently on the Executive Council (Exco), the Governor's appointed advisory board or "cabinet" <sup>3</sup>	Beijing had objected to the prospect that newly elected, liberal Legco members might be appointed to serve on Exco, giving them greater influence in the government
Draw most of the 800 members of the yet-to-be-formed "Election Committee" (which will select Hong Kong's Chief Executive) from the elected membership of the District Boards and Municipal Councils beginning in 1995 <sup>2</sup>	The Basic Law, which establishes the Election Committee, is silent on how its 800 members are to be selected; Beijing has assumed all 800 members would be appointed
Reduce the size of geographic constituencies for Legco elections and establish a system of one seat = one vote <sup>1</sup>	There are now 9 double-seat geographical constituencies where each elector can cast two votes, returning 18 members to Legco
Lower the voting age to 18 <sup>1</sup>	Currently the voting age is 21

<sup>1</sup> Proposal incorporated in the first legislative package passed on Feb. 23, 1994.

<sup>2</sup> Proposal incorporated in the second legislative package introduced on Feb. 25, 1994.

<sup>3</sup> Proposal enacted administratively by Governor Patten in 1993.

## Chinese Protests and Threats Over Patten's Proposals

From the outset, officials in Beijing swiftly and vigorously denounced Patten and his proposals, saying that they contravened the Joint Declaration and the Basic Law and were nothing short of an attempt to create new democratic institutions in Hong Kong where none existed before. China issued repeated personal attacks on Patten, and until the announcement of talks on Apr. 13, 1993, insisted that it would not negotiate with Britain about future political arrangements in Hong Kong until Patten withdrew his

proposals. Beijing maintained that any compromise short of withdrawal would be totally unacceptable.

In addition to objecting to the proposals themselves, Beijing objected to their consideration by Legco. Beijing has long opposed expanding Legco's jurisdiction beyond the limited powers it has had throughout Hong Kong's colonial history. Beijing prefers that Hong Kong remain a non-self-governing entity with the same kind of colonial administrative status the territory has had under British rule, although China has promised Hong Kong may have a "high degree of autonomy" and an independent judicial power. Chinese leaders consider it a bad precedent for Hong Kong's chief executive, in this case Governor Patten, to be held accountable to a decision by Legco -- probably suggesting Beijing's fear of future demands for autonomy or self-determination.

In addition to repeated rhetorical objections to the proposals, Chinese leaders threatened to take a number of retaliatory steps unless Patten backed down, including:

- Negate the Joint Declaration. China's Vice-premier Zhu Rongji, in London in November 1992 to meet with Prime Minister Major, was quoted as asking if both governments should tear up the Joint Declaration of 1984 which provides for the orderly transition of Hong Kong to China. While some have criticized the Joint Declaration, saying it is insufficient to protect Hong Kong's system and the Hong Kong people had no say in it, most believe it provides more certainty about Hong Kong's future than would no agreement at all. Zhu's remark, therefore, had an instant, negative impact on economic and political confidence in Hong Kong, and indicated the Chinese were prepared to intensify their objections to Patten's proposals.

- Dismantle Hong Kong's political institutions. In January 1993, Lu Ping, the Director of China's State Council's office of Hong Kong and Macau Affairs, warned that China would dismantle Hong Kong's political system in 1997 if Legco adopted Patten's proposals. Other Chinese officials have also mentioned this possibility, implying that China would set up a separate governing structure in Hong Kong now that would continue to function as Hong Kong's government after 1997. On occasions, Beijing also has stated that any Legco member voting for Patten's proposals will lose his or her seat when China resumes sovereignty. Britain has termed these threats to be a blatant disavowal of the Joint Declaration and the Basic Law, which declare that Hong Kong may keep its system for 50 years after 1997. China maintains that Britain is trying to change Hong Kong's system prior to 1997.

- Invalidate contracts for airport and container terminal construction projects. The dispute over Patten's proposals has become caught up in another ongoing Sino-British dispute over financing and construction plans for Hong Kong's mammoth, \$22 billion airport and container terminal construction projects, which the Hong Kong Government has been working on for years. China declared early in December 1992 that unless Patten's proposals are withdrawn, Beijing will consider all contracts signed for the projects prior to 1997 to be invalid unless they had first received Beijing's approval. British officials have reacted strongly to these threats, pointing out that under the Basic Law, China has promised to honor all contracts made before 1997. China's support for the airport is considered crucial for the project, since loan payoffs for the project's financing will extend well beyond 1997, when China resumes sovereignty. In other statements, Chinese officials declared that they will refuse permission to fly over Chinese airspace for flights originating from Hong Kong's new airport.



In a related move, China periodically also stated that it may not honor contracts for building Container Terminal #9, a planned new port facility, because the venture was not approved by Beijing. British officials have declared this a blatantly political move. Britain's Foreign Affairs Minister Alastair Goodlad stated that Britain had negotiated with the Sino-British Land Commission over the terminal project, and that the Chinese had approved the land grant for Container Terminal #9 on Mar. 20, 1992.

Britain and China were arguing about the airport project long before Patten announced his proposals. Although both governments have agreed in principle that Hong Kong's rapidly growing economy needs a larger airport and expanded port container capacity, Chinese officials have remained suspicious that major, lucrative construction contracts will be awarded mostly to British firms. They have been fearful that Britain will use the project to bleed Hong Kong of its rich cash reserves prior to 1997, saddling China with mammoth debt from the airport project. Because of these concerns, from the beginning China has questioned the scope of the airport project, criticized its financing plans, and insisted on being consulted about every aspect of its construction. Most observers understand China's definition of "consultation" to include the power to veto airport plans.

Frustrated with China's footdragging on the airport financing proposals, Britain in 1991 completed negotiations with Beijing on a Memorandum of Understanding (MOU) on the Airport Project. In the MOU, Britain conceded more oversight authority to Beijing in matters concerning the project; in exchange, China promised to adopt a "positive attitude" toward the project, and agreed to act swiftly in responding to the Hong Kong Government's construction and financing proposals. In September 1991, Prime Minister John Major became, reportedly reluctantly, the first Western leader to visit China after the Tiananmen Square crackdown. He went specifically to sign the MOU on the airport project. Some consider his distaste for this visit to have been the decisive factor behind Hong Kong Governor David Wilson's decision to retire shortly afterward, and Major's decision to select Patten as his replacement.

Despite the MOU, by late 1992 China had yet to approve any of Hong Kong's plans for financing the airport project. On Nov. 19, 1992, a month after Patten announced his proposals, the Hong Kong Government announced it could no longer delay, and would proceed with the \$1.2 billion site preparation phase of the project despite Beijing's refusal to approve the financing. Two weeks later, Beijing retaliated with its announcement that it would invalidate all contracts after 1997.

## **Prospects and Implications for Hong Kong**

### **Prospects for the Reform Package**

The initiation of talks on Apr. 22, 1993 suggested that both sides had made important concessions on the Patten proposals; China had dropped its refusal to take part in any discussions until Patten's proposals were withdrawn, and the Hong Kong Government seemed willing to delay the submission of the package to Legco if the talks progressed. But expectations fell as the negotiations dragged on with seemingly no progress. By early October, there was every indication that the talks were in trouble; at his second inaugural address, Patten signalled his intention to proceed with the proposals even absent Beijing's endorsement.

On Dec. 2, 1993, Patten announced that he would formally present part of the legislative proposals -- those portions that are less controversial -- to Legco on December 15, which he did. That legislation, which Legco passed on Feb. 23, 1994, lowered the voting age to age 18; created single-seat, single-vote elections for Legco, district boards, and municipal councils; and abolished appointed seats for local-level governing bodies. Legco's acceptance of the package raises the likelihood that it will accept the second and more controversial of Governor Patten's legislative proposals, announced on Feb. 24, 1994. The new legislation concerns the voting franchise for Legco elections scheduled for 1995; although Legco seats that would be filled by elections would remain limited, the number of Hong Kong citizens who could vote in those elections would be significantly expanded. It is the introduction of this more controversial proposal that prompted the Beijing to announce that after China resumed sovereignty over Hong Kong in 1997, it would dissolve Legco.

### **Prospects for Hong Kong's Political and Economic Future**

Hong Kong's stock market index, the Hang Seng, has alternately plunged and soared with each development in the Sino-British dispute, eroding the confidence of some about Hong Kong's political future as well as its future as a stable investment climate. The Hang Seng index, Hong Kong's stock market, has been volatile, first plummeting 25% from November 1 to Dec. 3, 1992, then rising to a record high (over 8,000) on Oct. 6, 1993, hours before Governor Patten delivered his second state-of-the-colony address. During a particularly vitriolic part of the crisis, in December 1992, Standard & Poor's put the Hong Kong Government on its Creditwatch, prompting some concern that Hong Kong's credit rating may be lowered in the future if the current dispute continues.

### **Possible Resolutions of the Current Impasse**

Given the economic and political stakes, the dispute over the Patten proposals has provoked widespread controversy within Hong Kong itself. Much of the Hong Kong business community has been instrumental in pressing both China and Britain to be flexible. This group has argued that no one gains by continued dissension, least of all Hong Kong, and that some kind of negotiation and accommodation ultimately is essential. Some have stated that Britain has no ultimate leverage in pushing the Patten reforms, since London will lose control over Hong Kong in 1997. A number of political and business groups in Hong Kong have taken the initiative to offer compromise alternatives and amendments to Patten's proposals to help resolve the dispute, and these groups appear to be discussing their initiatives with British, Hong Kong, and Chinese authorities.

With the rift between Britain and China continuing to grow, compromise on the dispute may be difficult, and any compromise would undoubtedly be subject to criticisms from various groups in Hong Kong and China. For instance, more liberal-minded Hong Kong citizens and Legco members -- in particular the United Democrats -- have criticized Patten and the British Government for not pushing harder on the reform package despite Beijing's reactions. They say China's uncompromising attitude proves that its leaders care little for the financial well-being of Hong Kong and its investors, and are prepared to damage Hong Kong's economy to undermine its government. They say that China's willingness to invalidate contracts after 1997 demonstrates it is not a trustworthy partner. Therefore, this group argues, the best protection for Hong Kong is to foster as much institutional autonomy as possible before British rule ends in 1997.

Others in Hong Kong, such as the political group called the Cooperative Resources Center, are generally supportive of China's position. This group argues that Chinese leaders are justified in their concerns about Patten's proposals. They say Britain is exploiting the gray areas of the Joint Declaration and the Basic Law in proposing the reforms, and is deliberately trying to create new democratic institutions and establish constituencies for self-governance. According to this group, Britain's actions are more appropriate for giving independence to a colony, not for handing over its sovereignty to another nation. Beijing, as the future ruler in Hong Kong, has every right to be consulted about the political structures it will inherit as the governing power.

### **Implications for "Greater China"**

The dispute over Patten's proposals for Hong Kong has wider economic and political implications for what is sometimes referred to as "Greater China" -- meaning the rapidly growing production zone encompassing Hong Kong, Taiwan, and the southern coastal areas of China. Hong Kong is by far the largest source of outside investment in mainland China. The economic cooperation of the three regions has grown enormously in the past decade, making "Greater China" the fastest growing economic area in the world. In large part, Greater China has come into existence because of Beijing's promises of "one country, two systems" for Hong Kong -- that is, that Hong Kong will have a high degree of autonomy and may keep its own economic, social, and legal system for 50 years after 1997. Investor confidence in the "Greater China" region could erode significantly or even halt for a time, along with economic growth, if Beijing continues to be judged willing to place ideology above economic interests. The "Greater China" region could also suffer if Beijing decides to promote investment alternatives to Hong Kong, such as Shanghai or Hainan Island.

### **Implications for Taiwan**

In theory, uncertainty over Hong Kong's future could also raise tensions between the PRC and Taiwan. Since the communist takeover of China in 1949 and the flight of the Chiang Kai-shek government to Taiwan, both Taiwan and China have adhered officially to a "one China" policy, each claiming that there is only one China and Taiwan is part of it. Chinese leaders have used their pledge of autonomy for Hong Kong as an incentive to convince Taiwan to reunify with mainland China under Chinese sovereignty. But as the wartime generation of leaders in Taiwan dies off, it has been replaced by a growing domestic movement in support of Taiwan's declaring itself to be independent of the PRC. If Beijing is to have any hope of defusing this growing sentiment, then at a minimum its promise of "one country, two systems" for Hong Kong must be viewed as credible.

### **Implications for Japan**

Japan vies with the United States as the external economic power having the most to gain or lose in the outcome of the current conflict between Britain and Beijing. Japan's past aggressiveness in pursuing Hong Kong and China-based investments has made it the first or second largest investor in the territory, not counting China itself. Annual new Japanese direct investment in Hong Kong peaked in 1989 and then began to decline somewhat, but still amounted to nearly \$1 billion in Japan's FY1991, with cumulative investment totalling \$10.8 billion.

Japan is pinning its investment hopes on the continuing rapid development of the South China coastal economic zone, with Hong Kong as its hub. China emerged in 1992 as the leading recipient of new Japanese foreign direct investment (FDI), as well as one of the top two recipients of Japanese economic assistance. Japan's economic importance to China could give it additional potential influence over Beijing's policies -- particularly in concert with U.S. action. At the same time, the success of Japan's investments in both entities will depend heavily on the continuation of economic reform in China, a stable economic symbiosis between Hong Kong and its supplier base, and a growing market in southern China. Japan is likely to have much less interest in democratization issues than does the United States. As a result, Japan could favor approaches to the Hong Kong-China problem that differ with those of the United States.

## **Implications and Options for the United States**

### **Current U.S. Policy and Actions**

Since Hong Kong has not been and -- under current agreements -- never will be a separate country, the question of how to deal with Sino-British disputes over the territory has been a difficult one for the United States. The U.S. attitude toward Hong Kong is viewed as inextricable from U.S. policy on China. In weighing decisions that affect American interests in Hong Kong, U.S. policymakers generally must strike a balance between protecting extensive U.S. business interests in Hong Kong and China, and maintaining support for human rights and democratic principles.

**The Bush Administration.** As did the Reagan Administration before it, the Bush Administration maintained a low profile on matters in Hong Kong, tending to acquiesce in British policy decisions. When pressed for U.S. policy on Hong Kong, Bush Administration officials generally referred to U.S. support for ensuring Hong Kong's continued stability and prosperity, and stated that future disagreements should be settled in a manner consistent with the best interests of the people of Hong Kong. As the dispute over the Patten proposals began, the U.S. Government position was reported to be that Patten's proposals were constructive and should be considered by all parties.

In December 1992, during her visit to China and Hong Kong, U.S. Secretary of Commerce Barbara Franklin took a stronger stand in asserting U.S. interests. The Secretary met with Premier Li Peng and Governor Patten, and made it clear to both that one of the key objectives of her visit was to express strong U.S. interest in seeing contracts honored in Hong Kong both now and after 1997. In Hong Kong, the Secretary underscored U.S. concern by touring the largest U.S. investment in the territory: the Sealand container terminal, which is the world's largest container facility. Sealand, a subsidiary of CSX Corporation, is also one of the bidders in the Container Terminal #9 project, contracts for which China has threatened to invalidate after 1997.

**Clinton Administration Policies.** Reacting in December 1992 to the growing Sino-British dispute over Hong Kong, President-elect Clinton stated his hopes that the United States could play a constructive role in relieving tensions and concerns in Hong Kong. Since then, however, the Clinton Administration has taken several tough actions against China which many believe could heighten tensions between the United States and China, possibly with repercussions for Hong Kong. On May 28, 1993, President Clinton issued a report to Congress and an executive order that placed human rights considerations

as a condition for renewal of MFN to China in 1994. On Aug. 24, 1993, the United States determined that China had sold M-11 missile-related equipment to Pakistan in violation of the Missile Technology Control Regime (MTCR) guidelines by which China had agreed to abide. Under the provisions of the Arms Export Control Act, which mandates sanctions in such cases, the United States has imposed Category II sanctions on China, banning for 2 years U.S. Government contracts and export licenses for missile equipment or technology, including licenses for satellite components.

**Congressional Action and Current U.S. Law.** Prompted by recurring Sino-British tensions, ongoing difficulties in U.S.-China relations, and the growing American economic presence in Hong Kong, Congress has focused more on Hong Kong in recent years. So far, the main thrust of legislation has been to provide for continuity in U.S. relations with Hong Kong after it reverts to Chinese control. In 1990, Congress enacted the Immigration Act of 1990, which established a separate immigrant visa quota for Hong Kong and offers a deferred visa to Hong Kong residents, thereby providing a possible future refuge without provoking an immediate exodus. In 1992 Senator Mitch McConnell, concerned over what he described as the complete lack of any U.S. policy for dealing with impending Chinese rule over Hong Kong, introduced legislation which set forth prescriptions for how the United States should conduct bilateral relations with Hong Kong as a non-sovereign entity. His bill (S. 1731), enacted as Public Law 102-383, does a number of things, including the following:

- Declares that support for democratization is a fundamental principle of the United States which should apply to U.S. policy toward Hong Kong after 1997.
- Declares congressional support for the Sino-British Joint Declaration, and makes a number of findings about what that agreement provides for, including the fact that Hong Kong's legislature (Legco) will be constituted by elections, and that all agreements the United States has implemented with Hong Kong by June 30, 1997, will continue in force after that date.
- Requires the United States to apply the same laws toward Hong Kong after 1997 as were in force before that date, but permits the President to suspend those agreements beginning July 1, 1997, if he determines that China is not giving Hong Kong sufficient autonomy.
- Requires the Secretary of State to report to Congress every 18 months on the situation in Hong Kong, including on the development of Hong Kong's democratic institutions.

In the 103rd Congress, Senator Connie Mack and Congressman John Porter, concerned about possible Chinese reprisals against journalists for their reporting, each introduced legislation that would provide a certain number of deferred visas to Hong Kong journalists and their families.

### **Hong Kong and Its Relation to U.S. Policy on China**

Given the very large U.S. economic presence in Hong Kong, an unfavorable or destabilizing outcome to the current Sino-British dispute would have significant negative implications for U.S. business interests in the territory. But a major complicating factor

for U.S. policy is the extent to which events in Hong Kong, and the U.S. response to those events, are linked to U.S. policy toward China and to U.S.-China relations.

**Most-favored-nation (MFN) Status For China.** Extensive economic interrelations between Hong Kong and China have made it virtually impossible for the United States to take an economic action regarding one that does not also affect the other. Over the past decade, Hong Kong has been able to greatly expand its production capacity by shifting most production facilities into mainland China. Many of these facilities are either producing goods under contract for U.S. companies, or else are owned, either partly or wholly, by U.S. concerns. Because of the close Hong Kong/South China connection, Hong Kong's economy and U.S. economic interests in the territory have become prominent features in the annual U.S. debate over whether to deny or place further conditions on MFN tariff status for products made in China. In MFN legislation of 1992 (H.R. 5318), Congress listed China's adherence to the Joint Declaration on Hong Kong as one of the conditions for continued MFN eligibility. In a statement of Dec. 3, 1992, Governor Patten stated that he did not want to see his political proposals linked to the MFN debate in the United States.

The current Sino-British dispute over Hong Kong could affect the U.S. MFN debate this year in several ways -- either by convincing U.S. policymakers to be tougher on China; by encouraging them to place even more conditionality emphasis on Hong Kong in an attempt to increase U.S. leverage over Beijing; or by persuading them to be more flexible on the MFN issue in order to provide some protection and support for Hong Kong. U.S. actions to deny or condition MFN for China also could influence the Sino-British dispute over Hong Kong, perhaps by convincing Beijing that it has nothing further to lose by holding firm against Patten's reform proposals. China also could retaliate later against U.S. actions on MFN by deciding to withhold approval for high-value contracts for which U.S. firms may want to bid on the airport and container terminal projects, or by imposing new conditions on the operations of U.S. businesses in China.

**China's Application to GATT.** China's pending application to the General Agreement on Tariffs and Trade (GATT) provides another possible leverage point for the United States in the current dispute over Hong Kong. During her visit to China in December 1992, U.S. Secretary of Commerce Barbara Franklin reportedly expressed the deep U.S. concern over Chinese officials' statements that contracts would not be honored after 1997, and some have speculated that China's application to become a member of the GATT will be held up until China gives assurances that contracts will be honored. The U.S. attitude toward China's GATT application -- and toward Taiwan's pending GATT application, which China opposes -- could have an impact on Beijing's reactions to Patten's proposals.

## **Prospects**

The standoff in Hong Kong places the Clinton Administration and Members of Congress in the difficult position of having to try to balance a number of competing U.S. policy goals. On one side are a set of issues involving U.S. economic interests and global economic competitiveness. Given the current emphasis on improving the U.S. economy, it may be politically difficult for policymakers to take actions regarding Hong Kong that could adversely affect U.S. economic interests there or in China. In fact, given the potential economic damage the Hong Kong dispute could cause, U.S. policymakers may be inclined to put pressure on Britain to come to some accommodation with Beijing. Confronted

with these economic imperatives, the Clinton Administration will also have to factor in an argument that many Americans make -- and that the President referred to in his own campaign promises -- that the United States should be doing more to employ workers at home instead of "exporting" American jobs overseas to manufacturing centers such as Hong Kong, China, and others.

On the other hand, others argue that U.S. investments overseas create American jobs and contribute to the American economy, and caution against any action that might jeopardize the situations of American companies in Hong Kong. To complicate matters further, U.S. policymakers must also consider the traditional U.S. emphasis on human rights and democratization. Since the collapse of Soviet communism, the United States and Members of Congress have placed great emphasis on committing U.S. resources to help establish democratic forms of government in former Soviet republics and East European countries. It may be difficult for policymakers who support such democratization initiatives to remain uninvolved while a capitalist and free Hong Kong is turned over to one of the last communist holdout states.

Finally, continuation of the dispute in Hong Kong may complicate U.S. policy decisions over the longer term because of the provisions of the U.S.-Hong Kong Policy Act. The law's requirement of a regular report to Congress on conditions in Hong Kong ensures that matters involving Hong Kong will continue to be raised in succeeding Congresses. And U.S. statements in the Act about what the Joint Declaration of 1984 means for future economic and political policies in Hong Kong are likely to be challenged by Beijing.

## **CHRONOLOGY**

- 02/24/94** -- China announced it would dissolve Legco and Hong Kong's municipal and district governing boards in 1997.
- 02/24/94** -- Patten proposed a second legislative package containing more controversial measures.
- 02/23/94** -- Legco passed the first of Patten's reform proposal bills.
- 12/15/93** -- The reform package was submitted to Legco.
- 12/02/93** -- Governor Patten addressed Legco, announcing that he would submit part of his legislative proposals to them for consideration on December 15.
- 11/27/93** -- The 17th round of Sino-British talks recessed without setting a date for an 18th meeting.
- 11/08/93** -- Governor Patten went to London to discuss the Hong Kong situation with Prime Minister Major and other British officials.
- 10/06/93** -- Governor Patten gave his second annual state-of-the-colony address in Hong Kong.

- 10/01/93** -- British Foreign Secretary Douglas Hurd and Chinese Foreign Minister Qian Qichen met for talks while attending the United Nations' foreign ministers meeting.
- 09/26/93** -- The twelfth round of talks began in Beijing.
- 05/04/93** -- Governor Patten, in the United States for a visit, gave an address at the National Press Club.
- 04/22/93** -- Sino-British talks began.
- 04/13/93** -- The British and Chinese governments jointly announced that talks on the dispute over Hong Kong will begin on Apr. 22, 1993.
- 03/30/93** -- Hong Kong's Executive Council (Exco) decided to wait until after Easter to decide on when to submit Patten's legislative proposal to Legco.
- 03/17/93** -- China renewed its threat to set up a shadow government in Hong Kong if Patten's proposals are accepted.
- 03/12/93** -- Patten announced to Legco that the British Government has been unable to reach agreement with the Chinese for negotiations over his proposals.
- 03/05/93** -- Patten addressed a special session of Legco to explain the delay in publishing or "gazetting" the reform proposals.
- 03/01/93** -- Members of a pro-China political group in Hong Kong, the Cooperative Resources Center, met with Premier Li Peng in Beijing about the Sino-British dispute.
- 02/28/93** -- Patten's stated deadline passed for submitting the reform package to Legco.
- 01/13/93** -- Legco rejected a proposal urging the Government to introduce the constitutional package outlined by Patten.
- 12/09/92** -- Patten said that Hong Kong would be adversely affected unless the United States renewed MFN for China unconditionally.
- 12/08/92** -- President-elect Clinton stated that he hoped the United States can play a constructive role in relieving tensions and concerns in Hong Kong.
- 12/03/92** -- The Hong Kong stock market was at approximately 5,000, down from about 6,300 on November 1.
- 12/01/92** -- The Journal of Commerce reported that China announced over the weekend it would not honor contracts for Hong Kong's new Container Terminal #9.
- 11/30/92** -- Chinese officials stated that all contracts, leases, and agreements signed or certified by the Hong Kong government without Beijing's approval would be invalid after 1997.



- 11/30/92 -- The tender period expired for the platform contract for the airport construction project.
- 11/27/92 -- China said that it may not honor the contract for construction of Container Terminal #9.
- 11/19/92 -- The Hong Kong Government decided to proceed with awarding the platform contract for the airport project, even absent Beijing's approval for the project's financing.
- 11/12/92 -- Chinese Vice-premier Zhu Rongji, in London to meet with Prime Minister John Major, asked if the Joint Declaration should "go with the wind."
- 11/11/92 -- Legco voted 32-21 to support Patten's reform proposals in general and promote further democracy in Hong Kong.
- 10/28/92 -- The Chinese and British Governments each published correspondence, exchanged during negotiations for the Basic Law, dealing with the arrangements for Hong Kong's elections in 1995.
- 10/24/92 -- A Chinese official, Lu Ping, said that unless Patten withdrew his proposals, China would not, after 1997, honor any contracts awarded for the airport project and would not permit flights originating from the airport to use Chinese airspace.
- 10/20/92 -- Patten went to Beijing for his first official visit to China.
- 10/07/92 -- Patten unveiled his five-year plan for democracy in his inaugural annual Policy Address in Hong Kong.
- 09/16/92 -- Hong Kong submitted to China new financing proposals for the airport project, revised in light of Beijing's earlier objections.
- 09/09/92 -- China submitted to Hong Kong its own version of financing proposals for the new airport.
- 05/92 -- The Hong Kong Government and the Provisional Airport Authority agreed in principle on a financial plan for Hong Kong's new airport.
- 07/10/92 -- Christopher Patten became the 28th Governor of Hong Kong.
- 09/91 -- Prime Minister John Major became the first Western leader to visit Beijing after Tiananmen Square. He made the trip to sign the Memorandum of Understanding on the Airport Project.
- 06/91 -- British and Chinese officials initialed a "Memorandum of Understanding" (MOU) on the new Hong Kong airport; among the things it contained was agreement that Hong Kong would allow greater participation by Beijing over planning for the airport, and Beijing in return would have a "positive attitude" toward the airport project.